(GP6581)

(4)

IN THE

Supreme Court of the United States

OCTOBER TERM, 1944.

No. 828.

DANIEL O. HASTINGS, as Special Trustee of Standard Gas and Electric Company, Debtor,

Petitioner,

against

HAYSTONE SECURITIES CORPORATION, a corporation of the State of New York,

Respondent,

and

H. M. BYLLESBY AND COMPANY; BYLLESBY CORPORATION; WALTER T. ROSEN, HARRY B. LAKE, PAUL MARSHALL ROSENTHAL, HENRY MARCH, JOHN ROSENTHAL and EDWARD E. THALMANN, as Co-Partners doing business under the firm name and style of Ladenburg, Thalmann & Co.; EDWARD E. THALMANN, as surviving executor of the last will and testament of ERNEST THALMANN, deceased; BENJAMIN S. GUINNESS; LOUIS M. LEVINE, ALMA METZ and HENRY L. MOSES, as executors of the last will and testament of Rudolph Metz, deceased; SIDNEY BACHARACH, VIRGINIA M. ROSENTHAL, PAUL M. ROSENTHAL, JOHN ROSENTHAL and FREDERICK M. HEIMERDINGER, as executors of the last will and testament of Moritz Rosenthal, deceased; FIRST SECURITY COMPANY, a corporation of the State of New York; AMEREX HOLDING CORPORATION, a corporation of the State of New York; UNION TRUST COMPANY OF PITTSBURGH, a corporation of the Commonwealth of Pennsylvania; STANDARD POWER AND LIGHT CORPORATION, a corporation of the State of Delaware; ARTHUR C. ALLYN; BERNARD F. BRAHENEY; JOSEPH H. BRIGGS; ORJA G. CORNS; ALBERT S. CUMMINS; HENRY C. CUMMINS; VICTOR EMANUEL; DENNIS T. FLYNN; ROBERT J. GRAF; E. CARLETON GRANBERY; JOHN L. GRAY; ROBERT G. HUNT; HENRY H. JONES; SAMUEL KAHN; WILLIAM C. LANGLEY; CHESTER C. LEVIS; DUNCAN R. LINSLEY; HERBERT LIST; BERNARD W. LYNCH; MATTHEW A. MORRISON; THOMAS A. O'HARA; JAMES F. OWENS; ROBERT F. PACK; WILLIAM G. POHL; JOHN P. PULLIAM; WILLIAM F. RABER; ROYAL E. T. RIGGS; ANDREW W. ROBERTSON; LOUIS H. SEAGRAVE; FREDERICK W. STEHR; T. BERT WILSON; ANNA G. BREWER, as Executrix of the last will and testament of Chauncey M. Brewer, deceased; and MARTIN J. O'BRIEN, as executor of the last will and testament of John J. O'Brien, deceased,

Defendants.

REPLY BRIEF IN SUPPORT OF PETITION FOR WRIT OF CERTIORARI.

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1. Respondent repeatedly asserts that the Court of Appeals held in the instant case that even if a judgment creditor had been the plaintiff, the statute of limitations would have barred the action. Thus respondent states (Br., p. 4):

> "The effect of the decision of the Court of Appeals was that, assuming that a trustee in bankruptcy had the rights, remedies and powers of a judgment creditor holding an execution duly returned unsatisfied, as contended by petitioner; and, assuming the suit was brought by such a judgment creditor under the State statute (Section 60, General Corporation Law), as contended by the petitioner; it was nevertheless barred by the State Statute of Limitations."

Again at page 5 of its brief, respondent criticizes petitioner's statement of the questions presented on the ground that

> "The Court of Appeals held explicitly that the action was equally barred whether maintained by a trustee in bankruptcy or a judgment creditor."

The Court of Appeals, however, made no such holding. Nowhere in its opinion did it state that the action would have been equally barred if it had been maintained by a judgment creditor. Respondent's reference to the Court of Appeals opinion in this connection is the following quotation therefrom, made at page 4 of Respondent's brief, immediately preceding respondent's assertion as to the Court's holding:

> "There would, indeed. be serious doubt whether a trustee in bankruptcy would have capacity to sue

> upon a cause of action which did not belong to the debtor other than a cause of action to set aside illegal transfers of property and unlawful preferences. (Citing cases.) We need not attempt to resolve that doubt in this case since we hold that under the law of the State the cause of action here asserted is based upon a wrong to the corporate debtor and accrued when the wrong to the debtor corporation was complete" (R. 86).

This quotation obviously does not state that the action would have been barred if maintained by a judgment creditor, as respondent asserts.

What the Court of Appeals does hold in the instant case is a twofold proposition: (1) that petitioner, although a trustee in bankruptcy, is limited to the rights and status of the debtor corporation because the facts alleged in the complaint constitute a wrong to the debtor corporation; and (2) that *Buttles* v. *Smith*, 281 N. Y. 226 (and the line of cases holding to the same effect) remain the law of New York. The necessary result of these two propositions is to deny to petitioner, as a trustee in bankruptcy, the rights and status which a judgment creditor would have been accorded as plaintiff in the instant action, in violation of the provisions of Section 70c of the Bankruptcy Act.

This is the necessary result because the purported distinction made by the Court, between the judgment creditor cases which were reaffirmed and the instant case, is entirely without substance. In *Buttles* v. *Smith* (*supra*), the facts alleged stated a wrong to the corporation. The action was based upon the transfer of corporate assets to the defendants in payment of personal obligations of the president. "Any action on behalf of the insolvent corporation to recover the funds would have been barred," as respondent admits (Br., p. 9). Nevertheless the judgment creditor was

held not limited to the rights of the corporation. Although the facts alleged constituted a wrong to the corporation, the judgment creditor's action was held to have accrued only after judgment was obtained with execution returned unsatisfied, not at the earlier date when the wrong to the corporation occurred.

The doctrine in *Buttles* v. *Smith* has been long recognized by the New York Courts. In *Shepard Co.* v. *Taylor Publishing Co.*, 234 N. Y. 465 (cited in the *Buttles* case), the Court expressly stated: "The corporation or its stockholders might have brought this action * * *". Yet the Court did not limit the judgment creditor to the rights of the corporation, but held that the statute commenced running only after judgment was obtained with execution returned unsatisfied. Likewise, in *Rosenkranz* v. *Doran*, 264 App. Div. 335, the payment of dividends out of capital created a cause of action enforceable by the corporation, as well as by its judgment creditors, under N. Y. Stock Corp. Law Sec. 58. Following the *Buttles* principle, the Court held that the judgment creditor's action accrued not when the wrong was done to the corporation, but years later when judgment was obtained and execution returned unsatisfied.

Since *Buttles* v. *Smith* is reaffirmed in the instant case, it is still the law of New York that a judgment creditor, even though suing on facts constituting a wrong to the corporation, is not barred by the statute of limitations applicable to the corporation. Hence the Court in the instant case denied petitioner the rights of a judgment creditor under State law, when it limited petitioner to the rights of the corporation on the ground that the facts alleged constituted a wrong to the corporation.

The opinion of the Court of Appeals attempts to formulate this purported distinction between the reaffirmed judgment creditor cases and the instant case as follows (R. 86):

> "The cause of action accrued to the debtor when the wrong occurred and though the statute permits a creditor or stockholder to bring an action for the wrong done to the corporation, the damage or injury to a creditor, like the damage or injury to a stockholder, *arises only indirectly from the damage or injury to the corporation and is repaired when the damage or injury to the corporation is repaired. That, as we have pointed out, was not true of the cause of action asserted in Buttles* v. *Smith* (281 N. Y. 226, *supra*), under a different subdivision of the same section of the statute." (Italics supplied.)

Contrary to the foregoing, both in *Buttles* v. *Smith* and in the instant case, the injury arose indirectly from the damage to the corporation and is repaired when the damage to the corporation is repaired. The injury (to the creditor in one case and the trustee in bankruptcy in the other) resulted indirectly from the reduction of the corporate assets which would have been available to pay the corporate debts; and the restoration of the corporate assets would have repaired the damage both to the corporation and the creditor and trustee in bankruptcy.

If a decision denies to a trustee rights which would have been accorded to a judgment creditor under state law, this Court is not precluded from so holding merely because the state court declares that there is a distinction between the trustee's action and the judgment creditor's action. To hold otherwise would permit the state court to pay lip service to Section 70e of the Bankruptcy Act, while in actuality disregarding its mandate. That, it is respect-

fully submitted, is the effect of the decision of the Court of Appeals in the instant case.

2. The respondent argues (Br., p. 12) that "Even if the decision of the Court of Appeals in this case were inconsistent with prior decisions, the question decided would still remain a question for the State court and not a federal question", quoting from *Patterson* v. *Colorado,* 205 U. S. 454, in support thereof.

This argument is misleading because based upon a misconception of petitioner's position. Of course, the reversal by a state court of prior decisions ordinarily raises no federal question. In *Patterson* v. *Colorado,* quoted by respondent, this Court held that a State court decision generally "is not an infraction of the 14th Amendment merely because it is wrong or because earlier decisions are reversed".

If in the instant case the Court of Appeals had held that hereafter judgment creditors suing on facts stating a wrong to the corporation would be limited to the rights of the corporation as to the statute of limitations, thereby reversing the doctrine of *Buttles* v. *Smith,* that would have presented no federal question. But the Court of Appeals did not reverse, but expressly reaffirmed *Buttles* v. *Smith.* The inconsistency here is between the reaffirmed decisions recognizing rights in judgment creditors and the instant decision denying the same rights to a trustee in bankruptcy in the same situation. That inconsistency does raise a federal question, since it involves a denial to a trustee in bankruptcy of rights vested in him under Section 70c of the Bankruptcy Act.

3. Respondent also argues (Br., pp. 13, 14) that petitioner may not complain as to the state court interpreta-

tion of N. Y. General Corp. Law Sec. 60 or the statute of limitations. Petitioner makes no such complaint, but accepts the state court interpretation of both statutes. All that petitioner asks is that he be accorded, pursuant to Section 70c of the Bankruptcy Act, the rights granted to a judgment creditor under the state court interpretation of those statutes. Petitioner does not question the power of the State to determine the applicable statute of limitations for any class of litigants. But he does question the power of the State, once it has granted certain rights to judgment creditors under the statute of limitations, to deny those rights to a trustee in bankruptcy.

4. Respondent asserts (Br., pp. 5-7) that the order appointing petitioner named him a "Special Trustee" and authorized him to sue only as to causes of action existing in favor of the Debtor. If respondent is here contending that petitioner is not a bankruptcy trustee, the clear answer is that the Court of Appeals rejected this same argument on a prior appeal in which the capacity of petitioner to sue was challenged (*Hastings* v. *Byllesby & Co.*, 286 N. Y. 468).

If, however, respondent is here arguing that even though petitioner was a trustee in bankruptcy, he did not become vested with the rights of a judgment creditor pursuant to Section 70c because he was authorized to sue only as to causes of action belonging to the Debtor, the answer is that as to these assets of the Debtor, the petitioner was vested with the same rights as any ordinary bankruptcy trustee. Petitioner was appointed "Special Trustee" because he did not obtain title to *all* corporate property; but as to that property which was vested in him (the prosecution of the specified actions), he became a bankruptcy trustee with full

title and status under Section 44 of the Bankruptcy Act, including the rights of a judgment creditor under Section 70c thereof.

5. Both the Court of Appeals (R. 85, 86) and respondent assert that petitioner's suit was brought solely on behalf of the corporation, to the exclusion of the rights of creditors. But, as just shown, the petitioner was vested with all of the rights of a trustee in bankruptcy as to the causes of action in question, including the rights of a judgment creditor pursuant to Section 70c. Nor did anything in the complaint state that petitioner sued solely on behalf of the corporation. On the contrary, the complaint expressly affirms petitioner's capacity as bankruptcy trustee and therefore, by necessary implication, his rights and status under the Bankruptcy Act, including those of a judgment creditor derived from Section 70c thereof.

6. Respondent asserts (Br., p. 11) that a cause of action accruing solely to the creditors of a corporation and not belonging to the corporation itself does not pass to a trustee in bankruptcy. Whether that is correct or not, it is not applicable in the instant case because the cause of action alleged by the petitioner is not vested exclusively in the creditors of the debtor. General Corp. Law Sections 60(1) (2) and 61 (quoted in Appendix to Petition), under which the action is brought, authorize suit by both the corporation and its creditors to compel payment by directors and officers of assets acquired by them or lost through violation of their duties. It is elementary that a cause of action which is vested in the corporation, as well as in its creditors, passes to the trustee in bankruptcy of the corporation, who may enforce it for the benefit of both the corporation and its creditors (*Gochenour* v. *Cleveland Terminals Bldg.*

Co., 118 F. (2d) 89 (C. C. A. 6); *Stephan* v. *Merchants Collateral Corp.*, 256 N. Y. 418; *Cowin* v. *Jonas*, 293 N. Y. 838).

The mistake which respondent and the Court of Appeals make is to reason that *because* the action must be vested in the corporate debtor in order to pass to the trustee in bankruptcy, therefore the trustee enforcing such action is limited to the rights and status of the debtor. That is a *non sequitur* which would nullify the provisions of Section 70e of the Bankruptcy Act, vesting in a trustee not only the title of the bankrupt, but also "all the rights, remedies, and powers of a judgment creditor then holding an execution duly returned unsatisfied, whether or not such a creditor actually exists."

7. Respondent argues (pp. 7, 8) that the instant action is not brought under General Corp. Law Section 60 because the complaint made no reference to such statute. No such reference was required. The decision of the Court below was rendered on the basis that this was an action maintained under General Corp. Law Section 60 (R. 86). The law is well settled that a statutory cause of action is encompassed in a complaint which alleges the facts required to invoke the statute, notwithstanding that the statute itself is not mentioned (*Reynolds Investing Co., Inc.* v. *Reynolds*, N. Y. Law Journal, November 22, 1938, McLaughlin, J., aff'd 256 App. Div. 912, mdfd. on another point, 281 N. Y. 180; *P. G. Poultry Farm* v. *Newtown B.-P. Mfg. Co.*, 248 N. Y. 293, 297).

Following the same line, respondent asserts (Br., pp. 7-9) that petitioner's contention that the instant action was brought under General Corp. Law Section 60 was an afterthought. This statement is incorrect and is unsupported by any reference to the record.

Conclusion.

Under the decision of the Court below, trustees in bankruptcy suing on the basis of state statutes conferring rights on both a corporation and its creditors would be limited to the status of the bankrupt corporation, even though a judgment creditor so suing would have enjoyed superior rights with respect to the statute of limitations. This is contrary to Section 70c of the Bankruptcy Act and the applicable decisions of the Courts. It involves a Federal question of substantial importance which calls for an authoritative ruling by this Court. The Petition for a writ of certiorari should be granted.

Dated: March 20, 1945.

Respectfully submitted,

DANIEL O. HASTINGS, as Special Trustee of Standard Gas and Electric Company, Debtor

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